United States Court of Appeals

for the Second Circuit

APPELLEE'S BRIEF

WRIT

75-6136 B

United States Court of Appeals

FOR THE SECOND CIRCUIT

NO. 75-6136

SOUTH WINDSOR CONVALESCENT HOME, INC.
Plaintiff-Appellee

vs.

CASPER WEINBERGER, SECRETARY OF HEALTH, EDUCATION AND WELFARE, THE UNITED STATES OF AMERICA AND TRAVELERS INSURANCE COMPANY
Defendants-Appellants

ON APPEAL FROM THE JUDGMENT OF THE [illegible]
DISTRICT COURT FOR THE DISTRICT OF [illegible]

BRIEF OF PLAINTIFF-APPELLEE

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PRELIMINARY STATEMENT

**Pursuant to Section 28,
Rules of the Court of Appeals
for the Second Circuit**

The decision appealed from was rendered by the Honorable T. Emmet Clarie, Chief Judge. The citation is *South Windsor Convalescent Home, Inc. vs. Weinberger,* 403 F.Supp. 515 (D. Conn. 1975).

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STATEMENT OF THE ISSUES

1. Did the District Court possess jurisdiction to render judgment in this action?

2. May the Secretary of Health, Education and Welfare constitutionally and lawfully recapture reimbursements for Medicare program participation *ex post facto?*

STATEMENT

Title XVIII of the Security Security Act, 42 U.S.C. Sections 1395 *et seq.,* commonly referred to as the Medicare program, is a federally funded health insurance program for the aged designed to provide health care services to qualified beneficiaries. The program is administered and funds are disbursed to the providers of those services in large part through state agencies and private organizations designated by the Social Security Administration as fiscal intermediaries. Under Medicare, post-hospital extended care is available to eligible beneficiaries in skilled nursing facilities such as those operated by the plaintiff in this action.

From November 22, 1966 until August 1, 1970, the provider reimbursement regulations [20 C.F.R. 405.415 (1970)] issued pursuant to Title XVIII by the Social Security Administration, and applicable to nursing homes, recognized an allowance for accelerated depreciation on capital assets as a reimbursable cost. Those regulations were effective for all cost reporting periods after January 1, 1967.

Under those regulations, nursing homes were given the option of using the straight-line, the declining balance, or the sum-of-the-years digits method of depreciation, and were permitted to use one of these methods of depreciation on a single asset or group of assets and another method on other assets. Reimbursement to nursing homes for accel-

erated depreciation allowances were determined by the fiscal intermediaries as an element of reasonable cost for the services rendered. Final settlements approving these amounts of reimbursement were made by the fiscal intermediaries with the providers for the years involved. *No provision existed in the regulations for a recovery of accelerated depreciation allowances upon withdrawal from the program.*

The Social Security Administration and the fiscal intermediaries approved these accelerated methods of depreciation for determining the useful life of an asset and openly encouraged their use as an acceptable accounting practice to enable nursing homes to obtain amounts of reimbursement that were sufficient to meet the principal amortization schedules for financing new construction, the expansion of existing facilities, and other expenses related to their participation in the Medicare program.

Beginning in 1969, the Secretary of HEW, through the fiscal intermediaries, began to cause the reduction of Medicare admissions to nursing homes by the imposition of more restrictive beneficiary eligibility requirements. This action resulted in substantial reductions in the number of Medicare patients eligible to receive skilled nursing care.

On August 1, 1970, the provider reimbursement regulations for Medicare were amended, in part, to delete an allowance for accelerated depreciation on capital assets acquired after that date, and by the addition of Section 405.415(d)(3) [20 C.F.R. Section 405.415(d)(3)]. This regulation provided that the accelerated method of depreciation could not be utilized by providers who enter the program after the effective date of the regulation. In addition, the regulation stated that if a provider which had been using the accelerated method of depreciation *terminated* its participation in the program after the effective date of the regulation, the difference between the reimbursement received by the provider utilizing the accelerated

method and what it would have received had it utilized the "straight-line" method would be recouped as an "overpayment" received by the provider during its participation in the program. 20 C.F.R. 405.415(d)(3) (1972).

Fiscal intermediaries thereafter began to recapture accelerated depreciation allowances previously paid or determined to be owed to nursing homes as a reimbursable cost for all cost reporting periods in which accelerated depreciation was claimed, which resulted in a retroactive application of the regulation for periods prior to its effective date. No determination was made that those allowances were in fact unreasonable costs.

This recovery of the accelerated depreciation allowances was made, in this instance, by threatening a cut-off of all federal funds due plaintiff from current payments owed it as provider of services under Title XIX of the Social Security Act, 42 U.S.C. Section 1396 *et seq.*, commonly referred to as the Medicaid program.

STATEMENT OF FACTS AND GENERAL DISCUSSION

The plaintiff, South Windsor Convalescent Home, Inc. (South Windsor), has participated in the Medicare program as a properly certified provider of skilled nursing care since July, 1969, pursuant to a provider agreement with the Secretary of HEW, which has been renewed annually until October 1, 1970, when plaintiff voluntarily terminated its participation in the program. The entire facility of the plaintiff was certified for use by Medicare patients at all times material to this action.[1]

On July 12, 1972 Travelers Insurance Company, the fiscal intermediary through which the plaintiff received its federal Medicare payments, notified the plaintiff that pursuant to 20 C.F.R., Section 405.415(d)(3), it was demanding pay-

[1] Affidavit of Francis F. Ronan, Rec. Doc. No. 9.

ment of $17,685.00 for accelerated depreciation in excess of straight-line amounts for the fiscal years ending September 30, 1967 through September 30, 1971 as follows:

Fiscal year ending	
September 30, 1967	$5,119.75
September 30, 1968	7,560.44
September 30, 1969	2,853.26
September 30, 1970	489.00
September 30, 1971	345.00
TOTAL	$16,367.45

Contrary to the assertion of the defendants that the fiscal intermediary "requested" repayment (Br. p. 6), the above amounts were recaptured from the plaintiff by the fiscal intermediary threatening the cut-off of federal financial participation in Title XIX of the Social Security Act, 42 U.S.C., Section 1396 *et seq.*, commonly referred to as the Medicaid program. This action, if carried out, would have denied the plaintiff payment for properly incurred expenses unrelated to the recapture dispute. Plaintiff would have been forced to close its door if payments due under the Medicaid program were cut off. No determination was made by the fiscal intermediary that these amounts of reimbursement were in fact unreasonable.

Pursuant to the threatened cut-off of federal financial participation in the Title XIX program which would have caused plaintiff undue hardship, plaintiff arranged for and paid the amount of $16,367.45 under protest.

Plaintiff instituted this suit to recover the sums paid under threat of cut-off of funds by the Federal Government.

The District Court held that Medicare regulation 20 C.F.R. Sec. 405.415(d)(3) was unconstitutional as applied to the plaintiff and designed to penalize the plaintiff for terminating its participation in the Medicare program. App. 21a, 25a.

The lower court's holding is broader than indicated by defendants-appellants (Br. p. 2). The Court having had the benefit of both the briefs and oral argument, held that recapture of depreciation charges taken prior to January 1, 1970 was both unconstitutional and unlawful. (App. 25a-26a).

The defendants' main argument is that the plaintiff will obtain a windfall if the Secretary does not recapture depreciation in excess of straight-line when the plaintiff terminated participation in the Medicare Program prior to the end of the useful life of its capital assets.

Defendants' arguments misfocuses this Court's attention by argumentative sleight of hand. Obviously a provider taking accelerated depreciation will have received more depreciation reimbursement during the first half of the useful life of its assets than if it had taken straight-line depreciation on equivalent value assets. The statutory mandate, however, does not direct the Secretary to choose the cost reimbursement formula resulting in the *smallest* reimbursement; rather, the Secretary is directed to provide any method or methods for a provider to approximate as closely as possible its actual costs of providing Medicare services. Defendants so concede (Br. pp. 19, 20). The question, therefore, becomes whether the accelerated depreciation method, viewed in the context of South Windsor's depreciable capital assets, provides a reasonable approximation of the actual depreciation of those assets. The defendants' Brief provides no insight whatsoever into that inquiry.[2]

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[2] The addendum is misleading. The hypothetical provider therein who took accelerated depreciation and remained in the program is not *required* to switch from accelerated depreciation to straight-line depreciation in 1972, as the Government seems to suggest. In fact, under 20 CFR 405.415(d)(2), the provider has the option of continuing to take accelerated depreciation or to switch to straight-line. Had the hypothetical provider continued taking accelerated depreciation, its 1972-1976 depreciation charges would have been as follows: 1972, $6,554; 1973, $5,243; 1974, $4,194; 1975, $3,355; 1976, $2,684. The provider's ten-year depreciation charges would

The defendants make much of the assertion that a terminating provider who has received accelerated depreciation charge reimbursement necessarily subsidized non-Medicare patients with Medicare funds. At the threshold, this assertion is patently false. Those providers who devote 100% of their facilities to Medicare patients obviously have no non-Medicare patients to subsidize. The record contains no showing of the percentage of Medicare patients serviced by South Windsor. The defendants would have this Court believe that the depreciation recapture regulations is designed to invalidate the accelerated depreciation method in all cases where "impermissible subsidization" has occurred. The argument is false.

The regulation [20 C.F.R. 405.415(d)(3)] does not visit recapture upon a provider who *sells* program capital assets and replaces those assets with equivalent assets. A provider who had received accelerated depreciation reimbursements on its program facilities is free to sell those facilities halfway through their useful life and to replace those facilities with equivalent facilities without suffering depreciation recapture under this regulation. This situation is illustrated in the Addendum to this Brief. Under the hypothetical facts presented in the Addendum, the provider who sells and replaces a program asset would receive, without recapture, some $17,232.00 more than the provider who utilized straight-line depreciation. The regulation simply is not directed toward the "evil" suggested by the defendants.

Indeed, if the defendants were correct in their statement of the administrative purpose behind the regulation and of the financial evil intended to be remedied, the regulation

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thus total $89,262, some $10,738 less than total straight-line depreciation. The regulations *continue* to sanction two different methods of determining depreciation reimbursement, which would result in demonstrably different total depreciation charges. This, of course, is in contradiction to the implicit proposition running throughout the Government's brief that the only depreciation methods currently sanctioned by the Secretary are those which, over the total useful life of program assets, will equate to straight-line.

irreconcilably conflicts with the provisions of 20 C.F.R. 405.415(f). That regulation provides in pertinent part:

> "(f) *gains and losses on disposal of assets.* Gains and losses realized from the disposal of depreciable assets while a provider is participating in the program, or within one year after the provider terminated participaton in the program, are to be included in the determination of allowable cost."

When this regulation is applied to the hypothetical provider above, that provider has a recognized "gain" (which in turn will affect allowable cost) *only* if the market value of the assets sold exceed their basis. The "market value" of the asset would be equal to original value less actual depreciation or loss of value, while the "basis" would be equal to original value less accelerated depreciation charges taken. In other words, this regulation resolves the issue whether accelerated depreciation charges approximate the actual cost of physical asset deterioration on a sale-by-sale basis, examining actual financial data. The regulation can operate only upon the assumption that accelerated depreciation charges may or may not be equal to actual depreciation in a given case. To the contrary, however, the depreciation recapture regulation as interpreted by the defendants operates only on the irrebuttable presumption that accelerated depreciation charges are *always* greater than actual depreciation. The defendants' interpretation would make the regulatory scheme both illegal and untenable, not to mention, inconsistent.

Defendants' Brief is replete with purported factual assertions which suffer dual shortcomings in that the assertions are (1) *dehors* the record and (2) factually incorrect.

The prime assertion which runs throughout is that the Secretary has determined that the only method of computing depreciation which approximates the statutory standard of "actual cost" reimbursement is the straight-line depreciation method. There is no evidence that the Secretary made such a determination. In fact, he did not.

The Secretary is required to promulgate Medicare regulations to reimburse providers, as closely as possible, for the actual costs of providing Medicare services for a given fiscal period. S. Rep. No. 404, 1965, US Code Cong. and Ad. News 1943, 1976 (89th Congress, First Session). The accelerated method of computing depreciation presumes that the usefulness of capital assets is depleted at a faster rate in earlier years than in later years. The Secretary, bound by the statutory standards of "actual cost" when authorizing use of accelerated depreciation, necessarily must have found that this depreciation method did approximate actual capital asset depletion for any given fiscal period. By continuing to allow the use of accelerated depreciation for providers who chose such method before August 1, 1970, the Secretary continues to recognize that this method furnishes an appropriate method of approximating actual depreciation costs.

Generally recognized economic and accounting principles validate the concept of accelerated depreciation. The Secretary was, and is, well aware of that general recognition, having had the benefits of the Report of the General Accounting Office to the Senate Finance Committee, Reimbursement Guidelines for Medicare, *Hearings Before the Senate Committee on Finance* (hereinafter *Hearings*), (89th Congress, Second Session), pp. 172-3:

> "The generally accepted definition of depreciation accounting is a system which aims to distribute the cost of an asset, less salvage, if any, over the estimated useful life of the asset in a systematic and rational manner. The accelerated depreciation methods provided for by principles have been generally recognized as meeting the test of being systematic and rational and have been accepted for use, subject to certain limitations and conditions, for Federal income tax purposes and for cost determinations under Federal procurement contracts. . . .
>
> ". . . (T)he basic rationale underlying the use of accelerated depreciation methods . . . is to the effect that

> the economic utility of an asset is relatively greater during the early years of its useful life, and accordingly relatively larger portions of the asset's cost should be assigned to the early periods of its use."

The record is barren of any evidence that a finding was made by the Secretary or his designee that the accelerated method of determining depreciation did not reasonably approximate the actual cost (physical deterioration and depletion of usefulness of capital assets) of South Windsor's particular operations. There is no evidence that South Windsor's physical plant actually deteriorated at a steady rate versus a decreasing rate. The defendants recognize that South Windsor is entitled to be reimbursed for "actual cost" of capital asset consumption. Without a factual showing in the record that South Windsor accelerated depreciation reimbursements unreasonably exceeded the actual cost of capital consumption, application of this regulation to South Windsor violates the statutory standard.

Viewed in the defendants' light, the focal point of the regulation becomes clear. Rather than operating upon a method of determining costs, the regulation instead focuses upon a provider's act of terminating program participation. An overpayment is said to have occurred in early years of participation only because of the subsequent act of termination, rather than because of the use of the accelerated depreciation method *per se*. Yet 42 U.S.C. Sec. 1395x(v), the source of authority for the regulation, does not permit the Secretary to make retroactive corrective adjustments based upon the act of termination, but only based upon a economically inappropriate "method of determining costs."

Defendants assert that the Secretary's decision to allow use of accelerated depreciation was based upon social and economic considerations similar to those underlying the allowance of accelerated depreciation for income tax purposes (Br. pp. 24-25). Defendants fail to recognize the

difference between the two statutory schemes. It has long been recognized that income tax legislation may be designed to fashion social and economic policy, *Ward v. Maryland,* 79 US 418, 427 (1871); *Couthoui, Inc. v. United States,* 54 F.2d 158, 163 (Ct Cl 1931). In contrast, the Secretary is limited to promulgating reimbursement regulations for the sole purpose of approximating the reasonable costs of providing Medicare services, 42 USC § 1395x(v).

ARGUMENT

I

JURISDICTION

The District Court did not lack jurisdiction to entertain this suit.

Defendants claim that jurisdiction is precluded under 28 U.S.C. 1331; the APA; 28 U.S.C. 1361 and exclusive jurisdiction by the Court of Claims. (Br. pp. 11, 17)

Defendants have omitted the most obviously grounds for conferring jurisdiction on a District Court.

> "The District Courts shall have original jurisdiction, exclusive of the courts of the state, of any action or proceeding for the recovery or enforcement of any fine, penalty, or forfeiture, pecuniary or otherwise, incurred under any Act of Congress". 28 U.S.C., Sec. 1355.

The plaintiff has alleged that it suffered a penalty imposed by the Secretary when it terminated its participation in the Medicare program. App. 6a.

The District Court held that the provision for recapture of accelerated depreciation under 20 C.F.R. 405.415(d)(3) was not authorized by statute and did in fact penalize the plaintiff for terminating its participation in the Medicare program. App. 21a, 25a.

The plaintiff has alleged the existence of a federal constitutional question in its complaint and supports jurisdiction by allegations that the defendants have deprived the plaintiff of property without due process of law by recapturing plaintiff's Medicare provider reimbursements pursuant to the provisions of an unconstitutional and unauthorized administrative regulation. These allegations sufficiently set forth a "statement of grounds upon which the court's jurisdiction depends" as required by Rule 8(a), Federal Rules of Civil Procedure.

A complaint need contain only a general allegation of the presence of a federal question supporting allegations of fact setting forth a right to recover under the Constitution or laws of the United States, *Bell v. Hood,* 327 U.S. 678 (1946).

In the *Bell v. Hood, supra,* case, plaintiffs' complaint contained a general allegation of jurisdiction followed by allegations that plaintiffs suffered damage as a result of being imprisoned by defendants in violation of plaintiffs' right to be free from deprivation of liberty without due process of law, and as a result of having their premises searched and their possessions seized in violation of their right to be free from unreasonable search and seizure. The Supreme Court reversed the lower court's dismissal of plaintiffs' claim for want of jurisdiction, stating, 327 U.S. at 681:

> "It is clear from the way it was drawn that petitioners seek recovery squarely on the grounds that respondents violated the Fourth and Fifth Amendments. It charges that respondents conspired to do acts prohibited by these amendments. . . . It cannot be doubted therefore that the pleaders propose to make violation of these Constitutional provisions on the basis of this suit."

A reading of plaintiff's complaint in the present case reveals an equally clear and plain statement of a suit based upon violation of plaintiff's Constitutional rights.

Defendants argue that the federal courts lack jurisdiction to review administrative determinations of reimbursable costs. Plaintiff raises no issue involving "an administrative determination of reimbursable costs". Plaintiff simply challenges the constitutional and statutory validity of a regulation and presents purely issues of law which involve neither administrative determinations of reasonable costs nor any other administrative determination of fact.

Plaintiff presents three jurisdictional claims in the present case:

A. That the administrative regulation involved herein deprived plaintiff of its property in violation of the Fifth Amendment;

B. That the regulation is without statutory authority; and

C. That the plaintiff was penalized for terminating its participation in the Medicare program.

No administrative body within the Medicare scheme is empowered to rule upon such issues of law. As to these issues, plaintiff has no "remedy" to exhaust within the administrative scheme. In such a situation, plaintiff may directly attack the constitutionality and statutory validity of this regulation without regard to the exhaustion doctrine. *United States v. Branigan,* 299 F. Supp. 225, 235-6 (SD NY 1969).

This exception to the exhaustion doctrine is eminently sound. The doctrine recognizes that the function and purpose of an administrative body is to apply administrative expertise to make factual determinations and conclusions within the body's area of expertise. Where, however, a particular issue is not within the authority of an agency to consider or decide, and where findings of fact are not necessarily ultimately to decide the issue, none of the purposes underlying the doctrine can be furthered by submission of that issue for agency determination.

In this case, plaintiff raises only issues of statutory construction and constitutional interpretation. No findings of fact are involved, and no agency discretion is involved. An administrative body lacks authority both to construe the extent of its statutory grant of authority, *Leedom v. Kyne,* 358 U.S. 184, 188-9 (1958) and to resolve constitutional questions, *Unglesby v. Zimny,* 250 F. Supp. 714, 717 (N.D. Cal. 1965).

Gar[illegible]le v. Richardson, 319 F. Supp. 16 (D. Mass. 1970) disposes of defendants' jurisdictional arguments. In that case, old age benefits of several Social Security recipients were reduced pursuant to a statutory provision deduction earned income from benefits otherwise payable. Plaintiffs sought damages, declaration and injunctive relief, and asserted the existence of federal diversity jurisdiction. Defendant moved for dismissal raising both the general doctrine of exhaustion and the specific prohibition of Section 405(h) of the Social Security Act. The Court found the defendants' arguments unconvincing *Id* at 18:

> "(1) Plaintiff Aims is not debarred from seeking judicial relief by the general doctrine that he must first exhaust his administrative remedies, nor by the more specific provision of Section 205(h) of the Social Security Act, 42 U.S.C., Section 405(h). The general doctrine is inapplicable because here plaintiff claims that the statutory provision permitting deduction is unconstitutional. Where a plaintiff attacks the constitutionality of the statute under which an administrative agency acts, and the attack does not turn upon a factual determination requiring administrative expertise, the doctrine of exhaustion of administrative remedies does not apply. *Public Utilities Commission of Cal. v. United States*, 355 U.S. 534, 539, 78 S. Ct. 446, 2 L. Ed. 2d 470; *Oestereich v. Selective Service Board*, 393 U.S. 233, 242, 89 S. Ct. 414, 21 L. Ed. 2d 402."

In *Aquavella v. Richardson*, 437 F.2d, 397 (2d Cir. 1971), a suit was brought against the Secretary of HEW and Aetna Life and Casualty Company as fiscal agent of the Secretary for damages and injunctive relief when payments under the Medicare Act to the plaintiff's nursing home were suspended pending an audit to determine whether or not over-payments were improperly made. The District Court dismissed the complaint for lack of jurisdiction on the grounds that the Medicare Act, 42 U.S.C., Section 1395-1395 11., precluded judicial review and that the suspension of payments was not final action under Section 10 of the Administrative Procedure Act, 5 U.S.C. Section 701-706.

However, the Circuit Court, in the *Aquavella* case, *supra,* disagreed with the government's contention that Section 405(h) operates as an express preclusion of judicial review and that the Medicare Act does not provide for review of a suspension of payments. The Court, affirming *Cappadora v. Celebrezze,* 356 F.2d 1 (2d Cir. 1966), stated at pages 401, 402, that the more reasonable construction of Section 405(h) is that it does not preclude judicial review.

The Court, in *Aquavella v. Richardson, supra,* also considered the question of whether the suspension of payments was a final action under the APA:

> ". . . there are no procedures either in the Medicare Act or in its regulations, by which appellant can secure administrative review of the suspension (citations omitted). Without judicial intervention at this stage, appellant is at the mercy of the Secretary who can insulate the allegedly illegal suspension from review by refusing to take any further action. To deny jurisdiction in this case is to hold the suspension unreviewable, perhaps forever." 437 F.2d at 404.

In *Aguayo v. Richardson,* 473 F.2d 1090 (2d Cir. 1973), plaintiffs sought to enjoin the government from carrying out two experimental work project programs which required the approval of the Secretary of Health, Education and Welfare under provisions of the Social Security Act, 42 U.S.C., Section 1315. The Court, at 1101, stated that Section 10 of the APA was an affirmative grant of jurisdiction.

County of Alameda v. Weinberger, 520 F.2d 344 (9 Cir. 1975), was a case where the State of California sought an injunction prohibiting the department of HEW from deducting portions of overpayments from its current quarterly grants to the State. HEW argued that Congress foreclosed judiciary review of disallowance determination thereby removing them from the purview of the Administrative Procedure Act [5 U.S.C., Section 701 (1) (1)]. The

Court stated that it disagreed with the contention of HEW because the controlling principle is that judicial review of final agency action shall not be deemed foreclosed unless Congress has forbidden review in unmistakable terms.

Ortego v. Weinberger, 516 F.2d 1005 (5th Cir. 1975), was another case where the Court held that APA, 5 U.S.C., Section 701, provided the basis for review of a decision not to reopen.

The *Ortego* Court, *supra,* 1007, noted that four out of five Federal Courts of Appeals have held that Federal Courts have jurisdiction to review, for abuse of discretion, the Secretary's decision not to reopen prior applications. These are the First Circuit, the Second Circuit, the Third Circuit and the Sixth Circuit. The Court, in the *Ortego* case, *supra,* agreed with the Second Circuit in *Cappadora v. Celebrezze,* 356 F.2d 1 (2d Cir. 1966) which relied upon various provisions of the APA as giving grounds for judicial review. The Court further stated, at page 1009, that

> ". . . the finality provision of the Social Security Act, 42 U.S.C., Sec. 405(h), does not preclude judicial review in the present case, because it applies only in situation where the aggrieved applicant has timely requested a hearing. A statute must demonstrate clear and convincing evidence of an intent to preclude judicial review before courts will cut off an aggrieved party's right to be heard."

Sanders v. Weinberger, 522 F.2d 1167 (7th Cir. 1975) also takes the position it will likewise follow the Circuits which hold that the APA, 5 U.S.C., Sec. 701-706, contain and independent grant of subject matter jurisdiction and that Sec. 405(h) of the Social Security Act does not bar review under the APA. This Court considered *Weinberger v. Salfi,* 422 U.S. 749 (1975) and determined that *Salfi* did not consider the review provision of the APA, but found that review was proper under Sec. 405(g) of the Act. 522 F.2d at 1171.

The Government takes the position that *Weinberger v. Salfi, supra,* precludes all judicial review under any claim arising out of the Medicare Act.

This interpretation is given short shrift by the subsequent Court decisions concerning this matter. *Sanders v. Weinberger, supra, Lejeune vs. Mathews,* 256 F.2d 950 (5th Cir. 1976). In *Lejeune v. Mathews, supra,* the Secretary urged the Court to hold that the District Court lacked jurisdiction to review the 1974 refusal to reopen a determination. The Court stated, at page 942, that this argument is foreclosed by the recent decision in *Ortego v. Weinberger* which held that a Federal District Court had jurisdiction under Section 10 of the Administration Procedures Act to review, for abuse of discretion, a refusal by the Secretary to reopen an application for Social Security benefits.

The Court, in *Lejeune v. Mathews,* stated,

> "The Secretary admits that if *Ortego* is good law, it controls the jurisdictional question in the case before us. The Secretary's argument is that *Ortego* was incorrectly decided in light of *Weinberger v. Salfi,* 1975, 422 U.S. 749, 95 S. Ct. 2457, 45 L. Ed.2d 522, a Supreme Court decision handed down shortly before *Ortego.* This argument is unavailing — *Salfi* was considered by the *Ortego* panel. See 516 F.2d at 1011, n.4, and we are bound by *Ortego's* construction of *Salfi.*" 256 F.2d at 953.
>
> "The law of this Circuit, then, is that a federal district court can have jurisdiction under the Administrative Procedures Act to review, for abuse of discretion, a decision by the Secretary not to reopen a determination of ineligibility for Social Security benefits. The District Court correctly applied the abuse of discretion standard to the facts of this case in the following manner." 256 F.2d at 953.

Plaintiff has proceeded directly to the only forum authorized to rule upon the constitutional and statutory challenges forming the basis of plaintiff's complaint.

Plaintiff has no administrative remedy to exhaust. It seeks to have a regulation declared unconstitutional as to it and to recover a penalty exacted by the Government for its act of termination. Plaintiff's claims are properly before this Court.

ARGUMENT

II

A. The regulation, applied retroactively, deprives South Windsor of property without due process.

A Medicare provider's right to reimbursement for costs incurred in providing Medicare services is in the nature of an earned property right for which the due process clause provides protection, *Coral Gables Convalescent Home, Inc. v. Richardson*, 340 F. Supp. 646, 650 (S.D. Fla. 1972). The defendants do not deny that South Windsor rendered such services during the periods at issue, nor do the defendants deny that reimbursements for accelerated depreciation charges taken during those periods were properly payable to South Windsor under the existing regulations.

Retroactive regulations are those which "take away or impair a vested right acquired under existing laws or create a new obligation or impose a new duty or attach a new disability in respect to transactions or considerations already past." *Vail v. Denver Building & Construction Trades Council*, 115 P.2d 389, 393 (Colo. 1941). While not all retroactive enactments are void, those enactments violate the due process clause which impair rights "which can truly be said to be *vested* rights of a nature constituting property rights." *Seese v. Bethlehem Steel Company*, 74 F. Supp. 412, 417 (D. Md. 1947).

In *United States v. Hudson*, 299 U.S. 498, 500 (1937), the United States Supreme Court recognized that Congress had the authority to create a limited period of retroactivity

for income tax legislation consistent with the due process clause:

> "As respects income tax statutes, it long has been the practice of Congress to make them retroactive for relatively short periods so as to include profits from transactions consummated while the statute was in process of enactment, or within so much of the calendar year as preceded the enactment; and repeated decisions of this Court have recognized this practice and sustained it as consistent with the due process of law clause of the Constitution."

The "recent transactions" test has been consistently applied, and constitutes a standard under which the present Medicare regulation cannot be countenanced.

The defendants misconstrue the focus of the inquiry required by the Supreme Court. Rather than examining the effects upon South Windsor created by the retroactive imposition of this regulation, the defendants consider only the situation in which the Secretary assertedly found himself and which triggered the promulgation of this regulation. In contrast, numerous cases give prime consideration to the nature and impact of the tax as it affects the taxpayer. See *e.g., Welch v. Henry,* 305 U.S. 134, 147-8 (1938); *Untermyer v. Anderson,* 276 U.S. 440, 445-6 (1928); *Nichols v. Coolidge,* 274 U.S. 531, 542 (1927); *First National Bank in Dallas v. United States,* 420 F.2d 725, 730-1 (Ct. Cl. 1970).

Defendants attempt to soften the statutory and regulatory effects on South Windsor to transform it into being neither harsh nor oppressive. That attempt was and is no substitute for the facts. All providers knew that the Secretary had passed cost reimbursement regulations defining how they were to be reimbursed for Medicare services. Whether the Secretary's 1966 authorization of accelerated depreciation was "controversial" is irrelevent to our issues; the relevant and undisputed fact is that this method *was*

authorized to providers such as South Windsor. How can the Secretary's authority to make "suitable" retroactive corrective adjustments require that South Windsor should have anticipated that the Secretary would attempt to reach, by retroactive regulation, beyond a provider's current program period? The provider's understanding of regulatory recapture was in the context of other retroactive adjustment regulations, 20 C.F.R., Sec. 405.454(b) and 20 C.F.R., Sec. 405.454(f)(1) promulgated November 22, 1966. These regulations both incorporate the maximum period of retroactivity — the current program year.

As to what the providers should have expected, one need only consider the statements of Robert M. Ball, then Commissioner of Social Security, *Hearings* p. 119:

> "Senator ANDERSON. What does the law require?
>
> Mr. BALL. That we pay cost.
>
> Senator ANDERSON. If you find out you haven't paid cost -- you have to pay it then. Why don't you find out about it?
>
> Mr. BALL. I don't think that the retroactive provision (42 U.S.C., Sec. 1395x(v)) contemplates going back over the year and changing the principles. I think what is contemplated is that you pay first on the basis of advances, that is estimates — not advances — an estimate —
>
> Senator ANDERSON. No, 'advance' is all right. I follow you.
>
> Mr. BALL. We have changed that. That is not an advance. But you make an estimate at the beginning of the year on the basis of these principles. Then at the end of the year you settle up, on the basis of the principles put out. It would hardly seem reasonable at the end of the year, after hospitals had entered into an agreement with you on the basis of certain principles, to shift all the principles for retroactive settlement in terms of how you compute a cost. I don't think that was contemplated at all."

The defendants' final proposition that South Windsor could have left the program after publication of the proposed regulation but before the regulations' effective date is demonstrably false. The termination regulation then in effect, C.F.R., Sec. 405.613(1970), provided as follows:

> "(a) A provider may terminate a section 1866 agreement by filing with the Secretary a written notice of its intention to terminate such agreement. The notice of intent to terminate should state the date for the termination of the agreement (the date must be the first day of a month). The Secretary may accept the termination date stated in the notice or he may set a different date. If the notice of termination does not specify the date for the termination of the agreement, the date is to be set by the Secretary. However, such date shall not be more than 6 months from the date the notice is filed. In addition to giving notice to the Secretary, the provider should also give at least 15 days notice to the public by publishing in one or more local newspaper a statement of the date of termination of the provider agreement with the Secretary. The notice also should inform the public of the applicability of termination (see Sec. 405.615) as it relates to the services of the provider.
>
> "(b) The Secretary may accept a notice of termination which is filed by a provider less than 6 months before the termination date, if the Secretary determines that to do so would not unduly disrupt the furnishing of services to the community serviced by the provider or otherwise interfere with the effective and efficient administration of the health insurance benefits program provided by Title XVIII of the Act. If the notice of termination is accepted by the Secretary, the provider should also give notice to the public in accordance with the provisions of paragraph (a) of this section."

The regulation generally provided for a minimum six-month period between date of notification of intent to terminate and date of actual termination. Even if South Windsor had submitted written notice on February 5, 1970, the date

the proposed regulation was first published, South Windsor's request for termination prior to the August 1 effective date of the regulation would have been disallowed unless the Secretary's required regulatory determinations were favorable to South Windsor. Thus, there was no way that South Windsor could have insisted on termination prior to the effective date of the regulation in question.

The defendants' reference to the admonition of *Federal Housing Administration v. The Darlington, Inc.*, 358 U.S. 84 (1958), is inappropriate. The legislative enactment in that case prohibited FHA mortgagors from renting FHA housing to transients only in the future, without attaching any consequences whatsoever to the mortgagors' previous rentals to transients.

> "The new Act applies prospectively only. So there is no possible due process issue on that score." 358 U.S. at 91.

In our case, of course, the regulation does not limit depreciation recapture to those charges taken subsequent to the enactment of the regulation, but purports to recapture depreciation reimbursements received over three and one-half years prior to the regulation's enactment.

An important factor in determining whether a legislative enactment may be given retroactive effect is the extent to which an affected party reasonably could have been expected to act differently had the party known that the legislation would be so applied. The outer limits of retroactive legislation are encountered in the income tax area, based upon the judicial assumption that the affected individual would not have altered his conduct whether or not the legislation applied to him.[3] This assumption, however, does not

[3] The Government (Br pp. 24-5) attempts to analogize the Secretary's introduction of accelerated depreciation into the Medicare Act with the introduction of that concept into the Internal Revenue Code. The Government fails to perceive the difference in purposes underlying the two statutory schemes. Furthermore, the analogy simply does not hold. On October 16, 1962, Congress enacted an accelerated depreciation recapture provision, the retroactivity of which was limited, 26 USC § 1245(a)(2)(A), to de-

hold in other areas, such as estate and gift taxation; see *Shanahan v. United States,* 447 F.2d 1082, 1083 (10th Cir. 1971):

> "However, the justification for upholding retroactive income taxation does not apply to estate and gift taxes because it cannot be assumed that the taxpayer would dispose of his property in the same manner if he had known about the consequences in relation to the tax."

In the present case, South Windsor began its program participation in July, 1967, and was given a choice of allowable methods of computing reimbursable depreciation charges, including straight-line and accelerated methods. Certainly no assumption can be made that South Windsor would have chosen the accelerated method, rather than the straight-line method, had South Windsor known that portions of its accelerated depreciation reimbursements would for many years remain subject to recapture in the event of future Secretarial whim.

It is settled law that regulations whose retroactive effect is harsh and oppressive are violative of due process. Both the record in our case and the applied authorities support the conclusion that the depreciation recapture regulation as applied to South Windsor transgresses Constitutional limitation.

B. The depreciation recapture regulation impairs the obligations of South Windsor's contract in violation of due process.

The defendants contend that the depreciation reimbursements previously paid to South Windsor, and which were recaptured from South Windsor, are not contractual payments, but rather statutory payments. This contention is unsound. First, *Coral Gables Convalescent Home Inc. v. Richardson,* 340 F. Supp. 646, 650 (S.D. Fla. 1972) rec-

preciation charges taken subsequent to December 31, 1961 – consistent with the "recent transactions" test of *United States v. Hudson, supra,* 500. In contrast, the recapture regulation as promulgated by the Secretary reaches far beyond the due process limitations respected by Congress.

ognizes that a provider of Medicare services receives "compensation for services rendered the Government." That the measure of compensation is specified by regulation rather than by explicit contractural provision does not dictate that the provider has no contractual right to receive this compensation. Any doubt to that effect is dispelled by *Johnson v. United States,* 79 F. Supp. 208, 210 (Ct. Cl. 1948). In that case, plaintiff was appointed a Federal District Court Judge when Section 260 of the Judiciary Code (28 U.S.C., Sec. 371) provided for continuation of salary upon retirement of any Federal Judge. Plaintiff subsequently retired, and shortly thereafter Congress purported to annul Section 260 insofar as it applied to plaintiff. The Court considered the question whether section 260 formed a part of plaintiff's contract of employment. The Court found that the statutory guarantee of lifetime salary was a part of plaintiff's contract, as "consideration offered to induce him to give up his right to hold office as long as he lives." Further, the Court expressed grave doubt as to the ability of Congress to retroactively deprive plaintiff of this contractual right:

> "Indeed, it is doubtful if Congress could take that right away from a judge, who had previously resigned under the above recited circumstances, by a repeal of the statute giving the right. Certainly a state cannot by the repeal of a statute relieve itself of a contractual obligation embodied in the statute repealed. (citation omitted). . . .
>
> "The right acquired by a judge who resigned after the passage of the Act sued on is no less a property right than the franchise granted to (a) company. Both, it would seem, come within the protection of the 5th Amendment." 79 F. Supp. at 211.

South Windsor's right to receive accelerated depreciation reimbursements is no less contractual for having been an "obligation embodied in the statute". In 1967, plaintiff contracted with the Secretary to provide medical care for

Medicare recipients, without further charge to the recipients of those services. In exchange, the Secretary contracted to pay plaintiff its "reasonable costs" which were specified by regulation. On plaintiff's entrance into the Medicare program, the regulations which formed a material part of plaintiff's contract (1) permitted plaintiff to take accelerated depreciation without any qualification on use of that method and without any recapture provision, and (2) contained no limitation on South Windsor's right to terminate program participation. More than three years later, on August 1, 1970, the Secretary by means of the depreciation recapture regulation not only altered, but retroactively emasculated both of these contractual provisions.

It is of no little significance that South Windsor is subject to the regulatory power of the Secretary *only* because of the above contractual relationship. The defendants' source of regulatory power over South Windsor does not emanate from the police power, war powers, emergency taxation powers, or any other "paramount power." This realization is significant, for as pointed out in *Lynch v. United States,* 292 U.S. 571, 579 (1934);

> "Rights against the United States arising out of a contract with it are protected by the Fifth Amendment. . . . (t)he due process clause prohibits the United States from annulling (these contract rights), unless, indeed, the action taken falls within the federal police power or some other paramount power."

There can be little doubt of the impairment of South Windsor's vested contractual right to retain accelerated depreciation charges received for past services. An impairment of contractual rights occurs. *Rorick v. Board of Commissioners of Everglades Drainage District,* 57 F.2d 1048, 1055 (N.D. Fla. 1932):

> "when the value of the contract has been diminished by subsequent legislation. The question of impairment is not one of degree, but of encroaching in any respect

upon the obligation — dispensing with any part of its force."

Prior to the effective date of the depreciation recapture regulation, South Windsor had fully performed past services for which it had received required reimbursements for accelerated depreciation charges. Subsequent to the regulation's enactment, South Windsor's right to those past depreciation reimbursements suddenly became subject to divestment should South Windsor *terminate* program participation.

The defendants urge that the Secretary was allowed to abrogate South Windsor's vested contractual right to retain past accelerated depreciation reimbursements because recapture was required to protect the integrity of the Medicare program.

This argument flies in the face of the Supreme Court's analysis in *Lynch v. United States, supra,* 292 U.S. at 580:

> "No doubt there was in March, 1933, great need of economy. In the administration of all government business economy had become urgent because of lessened revenues and the heavy obligations to be issued in the hope of relieving widespread distress. Congress was free to reduce gratuities deemed excessive. But Congress was without power to reduce expenditures by abrogating contractual obligations of the United States. To abrogate contracts, in the attempt to lessen government expenditures, would be not the practice of economy, but an act of repudiation."

ARGUMENT

III

The regulation, insofar as it authorized recapture of reimbursements for depreciation charges taken prior to January 1, 1970, is in excess of statutory authority.

In addition to its constitutional challenges, South Windsor contends that the depreciation recapture regulation exceeded the Secretary's statutory authority. A party

successful in the District Court is entitled to have its judgment affirmed on any ground finding support in the record. *Jaffke v. Dunham,* 352 U.S. 280, 281 (1957); *Lum Wan v. Esperdy,* 321 F.2d 123, 125 (2nd Cir. 1963).

Under the retroactive rulemaking statute, 42 U.S.C., Sec. 1395x(v), the Secretary is authorized only to make *suitable* retroactive corrective adjustments. Defendants do no contend otherwise. Instead defendants urge (Br. p. 26) that the depreciation recapture regulation, reaching back over three and one-half years in its application to South Windsor is a "suitable" retroactive adjustment authorized by Section 1395x(v). Textual logic and the law disagree with defendants.

In *Mount Sinai Hospital of Greater Miami, Inc. v. Weinberger and Blue Cross of Florida, Inc.,* 376 F. Supp. 1099 (S.D. Fla. 1974), a Medicare provider brought an action challenging the Government's attempt to recover payments for past services which the Government subsequently decided were not covered by the Medicare program. Based upon a 1972 review of the provider's Medicare services utilization for the years 1966-72, the Government determined that the provider had received over $6,000,000.00 in overpayments, and in May, 1973, notified it that portions of current reimbursements would be suspended to effect a recoupment.

The Government contended that Section 1815 of the Medicare Act (42 U.S.C., Sec. 1395g), providing for payment of providers for services rendered "with necessary adjustments on account of previously made overpayments or underpayments", authorized the Secretary to determine that services rendered in earlier program years, then classified as covered, were, in fact, not covered. The Court rejected this argument, finding that the scope of the Secretary's authority to make retroactive determinations was limited by the provisions of Section 1861(v) of the Act [42 U.S.C., Sec. 1395x(v)]:

"More importantly, Section 1861(v) clarifies the intended scope of the Secretary's authority under Section 1815 to make 'adjustments' for overpayments or underpayments. It not only contemplates, but expressly mandates, that provision be made in the Medicare regulations for 'suitable retroactive *corrective adjustments* where, for a provider of services *for any fiscal period,* the aggregate reimbursement produced by the methods of determining *costs* proves to be either inadequate or excessive.' Thus, the adjustments envisioned by the Act are intended only to reconcile amounts to be due as reasonable costs with amounts actually paid on the basis of cost estimates at the end of the fiscal period." (Footnote omitted, emphasis in original). 376 F. Supp. at 1128.

Addressing itself to the precise statutory question raised in the present case, the Court held that the scope of any retroactive corrective adjustment under Section 1861(v) was textually limited:

"Secondly, the retroactivity intended by Section 1861(v) to be accorded corrective adjustments is limited by its terms to 'any fiscal period.' Although Section 1815 commits the question of a suitable period within which to complete reasonable cost determinations to the Secretary's discretion, he has exercised that authority. The initial regulations issued provided that 'interim payments to providers will be made for services throughout the year, with final settlement on a retroactive basis at the end of the accounting period.' Thus, although the Act contemplates that adjustments will be retroactive, retroactivity is limited to the 'end of the accounting period.' It does not appear to extend, as defendants would have the regulations extend here, to permit the reopening of final settlements consummated up to six years ago." (footnotes omitted) 376 F. Supp. at 1129.

The Court held that the statutory scheme of the Medicare Act prevented the government from exercising its common law right of recoupment, and entered a judgment permanently enjoining the Government from recouping payments made to plaintiff prior to January 1, 1972.

On appeal, the Circuit Court of Appeals held that the Medicare Act did not limit the governments common law right to recoup overpayments which were improperly made. 517 F.2d 329, 338, 339 (1975).

However, the Circuit Court, in the *Mount Sinai* case, *supra,* concurred in the District Court's reasoning.

> "Section 1395g is limited in its impact to cost determinations and does not touch coverage problems. Despite its general reference to 'overpayments,' similar to Section 1395gg(b), consideration of the Medicare Act as a whole shows that this section has much more limited scope than is contended for by the government. The District Court's opinion on this question correctly analyzes the statutory scheme. 376 F. Supp. at 1127-1129. Congress chose to pay providers only the 'reasonable cost' of services, to be determined at the end of each fiscal year." 517 F.2d at 335.

The *Mount Sinai* Court's reasoning is sound. The statute authorizes the Secretary to make only "suitable" retroactive corrective adjustments. In order to determine what period of retroactivity is "suitable," one must examine both the context in which the provider operates, and other regulations in which the Secretary has expressed opinions on the appropriate extent of retroactivity for other adjustments in reimbursement.

The provider's participation in the Medicare program is geared to the concept of a program for a fiscal year. A provider receives interim reimbursements no less often than monthly, 42 U.S.C., Sec. 1395g, based upon billings which are preliminarily determined to be a reasonable estimate of Medicare costs. At the end of the provider's program year, the Secretary conducts a final audit to determine whether the actual cost reimbursements required by the Act for that completed program year are more or less than the interim reimbursements previously received by the provider, 42 U.S.C., Sec. 1395g, 20 C.F.R. 405.454. Thus, the general cost reimbursement provisions of the Act place

the provider's final reimbursement status in limbo until the final fiscal audit at the end of the program year. The avowed purpose of the audit is to give finality to those cost reimbursements received during the program year covered by the fiscal audit. Any retroactive corrective adjustment regulation, to be "suitable" within this context, necessarily must reach back no further than the beginning of the current fiscal period or program year in which the regulation becomes effective. A regulation which reaches back further would destroy the finality intended to be achieved by the audit.

The Secretary, in related regulations, has recognized that this is the appropriate period of retroactivity. 20 C.F.R. 405.454(b) provides:

> "(b) *amount and frequency of payment.* Title XVIII of the act states that providers of services will be paid the reasonable cost of services furnished to beneficiaries. Since actual costs of services cannot be determined until the end of the accounting period, the providers must be paid on an estimated cost basis during the year. While the law provides that interim payments shall be made no less often than monthly, intermediaries are expected to make payments on the most expeditious basis administratively feasible. Whatever estimated cost basis is used for determining interim payments during the year, the intent is that the interim payments shall approximate actual costs as nearly as is practicable so that the retroactive adjustment based on actual costs will be as small as possible."

And 20 C.F.R. 405.454(f)(1)states:

> "(f) *retroactive adjustment.* (1) Title XVIII of the Act provides that providers of services shall be paid amounts determined to be due, but not less often than monthly, with necessary adjustments due to previously made overpayments or underpayments. Interim payments are made on the basis of estimated costs. Actual costs reimbursable to a provider cannot be determined until the cost reports are filed and costs are verified.

> Therefore, a retroactive corrective adjustment will be made *at the end of the reporting period* to bring the interim payments made to the provider *during the period* into agreement with the reimbursable amount payable to the provider for the services rendered to program beneficiaries during that period." (emphasis added).

Thus, both the general statutory setting and related regulations promulgated by the Secretary illustrate that the retroactivity of any corrective regulation must be limited to the beginning of a provider's current fiscal period of Medicare participation. The depreciation recapture regulation was applied to South Windsor to recover depreciation charges received since the inception of South Windsor's participation on July 1, 1967. Retroactive recapture beyond January 1, 1970 simply is not authorized by statute.

Congress itself well may have given this Court an indication that the depreciation recapture regulation is "unsuitable" in the extent of its retroactive reach as applied to South Windsor. In 1972, Congress amended 42 U.S.C., Sec. 1395gg to provide that no recovery of overpayment to a provider would be made unless the provider was at fault, and further provided that:

> "...(S)uch provider of services ... shall, in the absence of evidence to the contrary, be deemed to be without fault if the Secretary's determination that more than such correct amount was paid was made subsequent to the third year following the year in which notice was sent to such individual that such amount had been paid; except that the Secretary may reduce such three-year period to not less than one year if he finds such reduction is consistent with the objectives of this subchapter."

Thus, Congress has indicated that the Secretary may not reach back further than three years even to recover reimbursement payments which were incorrect when made. In the present case, the Government contends neither that

South Windsor's depreciation reimbursements were incorrectly requested or computed, n[illegible] South Windsor was "at fault" in electing to take ac[illegible]ated depreciation.

> "Subsequent statements of Congress about what it meant years earlier in enacting a law are 'entitled to great weight in statutory construction.' *Red Lion Broadcasting v. F.C.C.*, 395 U.S. 367, 380-381, 89 S. Ct. 1794, 1801, 23 L. Ed.2d 371, 383 (1969)." *Mount Sinai Hosp. of Gr. Miami Inc. v. Weinberger*, 517 F.2d at 343.

Further, the Secretary himself has limited to three years any recomputation of amount of program reimbursement received by a provider. 20 C.F.R., Sec. 405.499g provides:

> "(a) *Reopening a determination.* A determination on the amount of program reimbursement contained in a notice of program reimbursement may be reopened by the intermediary, either on its own motion or at the request of the provider, at any time within 3 years of the date of such notice to correct the amount of program reimbursement due the provider or due the health insurance program. No such determination may be reopened after such 3-year period except as provided in paragraph (d) of this section.
>
> ". . . .
>
> "(d) *Reopening because of fraud.* Notwithstanding the provisions of paragraphs (a), (b), or (c) of this section, a determination or a decision shall be reopened and corrected by the intermediary at any time it if is found that such determination or decision was procured by fraud or similar fault by the provider or any other person.
>
> "(e) *Applicability.* The provisions of this section shall apply to cost reporting periods ending on or after December 31, 1971. The provisions of this section shall also be applicable to any cost reporting period ending before December 31, 1971, and for any such period the 3-year period referred to in this section shall commence on the date of the intermediary's final determination on the cost report filed for such cost repo[illegible]ng period."

The administrative determination to recapture funds from South Windsor was made on July 12, 1972, more than three years after South Windsor had received all depreciation reimbursements and notices of program reimbursement for program years 1967 and 1968. Yet, the depreciation recapture regulation, as applied to South Windsor, would mandate recovery of depreciation payments for those two program years in contravention both of the general policy set by Congress and of the Secretary's own specific limitation regulation. Why does the law set a three year limit for errors, if the Secretary can hold South Windsor for five years without having erred?

Kingsbrook Jewish Medical Center v. Richardson, 486 F.2d 663 (2nd Cir. 1973), cited by defendants (Br p. 20), does not validate what the defendants urge for the depreciation recapture regulation. *Kingsbrook* recognizes that the Secretary is directed by statute to make suitable retroactive corrective adjustments. The issue as to what period of retroactivity would be suitable for any regulation under Section 1395x(v) was neither presented to the *Kingsbrook* Court nor decided. The *Kingsbrook* Court also recognized that a limitation of the period of retroactivity might be necessary without statutory limitations:

> "The Secretary also urges us to consider the hardship that would prevail if all reimbursements remained forever subject to adjustment. We recognize that this policy consideration may dictate a regulation which limits the extent of retroactivity." 486 F.2d at 670.

Kingsbrook further involved a formal, documented finding by the Secretary that the "single unit" method of cost calculation previously required by the cost reimbursement regulations was an unsuitable method for all providers across the board. In our case the depreciation recapture regulation focuses not upon an erroneous "method of determining costs" but rather upon a provider's act of termination. *Kingsbrook* does not sanction, much less compel,

a regulation that invalidates a cost determination method used by terminated providers while sanctioning the identical method for continuing providers.

The exact same set of facts, as in the present case, involving a controversy exceeding $10,000.00, and involving the same law were considered in the case of *Hazelwood Chronic and Convalescent Hospital, Inc. v. Weinberger,* Civil No. 73-210 (D. Ore., 1974), appeal pending, C.A. 9, No. 74-2210).

The Court, in the *Hazelwood* case, *supra,* concluded, Medicare regulation 20 C.F.R. 405.415(d)(3) is unconstitutional under the due process clause of the Fifth Amendment to the United States Constitution, to the extent that the the regulation authorized recapture of reimbursements for depreciation charges taken prior to the beginning of the year in which such regulation was promulgated.

CONCLUSION

The Secretary could not lawfully recapture accelerated depreciation reimbursements made to South Windsor for periods prior to January 1, 1970. The regulation as promulgated exceeds the Secretary's statutory authority under 42 U.S.C., Sec. 1395x(v) to make "suitable" retroactive corrective adjustments. The regulation deprives South Windsor of property with a degree of retroactivity exceeding that allowed by the due process clause of the Fifth Amendment, and unconstitutionally impairs South Windsor's Medicare contract rights. The decision of the District Court should be affirmed.

Respectfully submitted,

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ADDENDUM

$100,000 ASSET

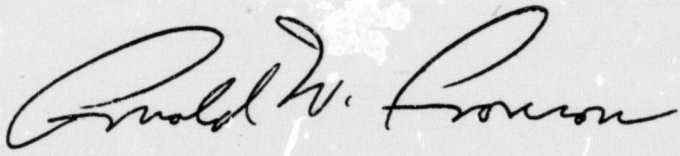
(10 Years Estimated Life)

Year	STRAIGHT-LINE		PROVIDER WHO LEFT PROGRAM IN 1971	PROVIDER WHO REMAINS IN PROGRAM 10 YEARS	
1967	$10,000		$20,000	$20,000	
1968	10,000		16,000	16,000	
1969	10,000		12,800	12,800	
1970	10,000		10,240	10,240	
1971	10,000		8,192 (Leaves Program)	8,192	
		Sub Total $50,000	Sub Total $67,232†		Sub Total $67,232
1972	10,000			6,954	(Switched to straight-line depreciation as provided by 20 CFR 405.415(d)(3)
1973	10,000			6,453	
1974	10,000			6,453	
1975	10,000			6,453	
1976	10,000			6,453	
	$100,000*			$100,000*	

*Depreciation per year $10,000

†Average depreciation in program for 5 years only would be $13,446.00 for one who leaves program early, but only $10,000.00 for both straight-line and accelerated depreciation for those who stay in program 10 years.

I certify that a copy of the foregoing Brief of plaintiff-appellee was served, on the 27th day of March, 1976, by mailing a true and correct copy thereof, certified by me as such, and deposited in the United States mail on said day with sufficient postage, in a sealed envelope at the post office in Hartford, Connecticut upon ROBERT E. KOPP, DAVID M. COHEN, DEPARTMENT OF JUSTICE, APPELLATE SECTION, Washington, D.C., 20530, attorneys for defendants-appellants, and SIDNEY I. LEZAK, PETER C. DORSEY, MARJORIE A. WILHELM, U.S. ATTORNEY'S OFFICE, P. O. Box 1824, New Haven, Connecticut 06508, attorneys for defendants-appellants.



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